

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN EXAMINATION BY THE PUBLIC SERVICE)
COMMISSION OF THE ENVIRONMENTAL)
SURCHARGE MECHANISM OF KENTUCKY) CASE NO. 2010-00474
UTILITIES COMPANY FOR THE SIX-MONTH)
BILLING PERIOD ENDING OCTOBER 31, 2010)

O R D E R

On December 27, 2010, the Commission initiated a six-month review of Kentucky Utilities Company's ("KU") environmental surcharge as billed to customers for the six-month period beginning May 1, 2010 through October 31, 2010.¹ Pursuant to KRS 278.183(3), the Commission must review, at six-month intervals, the past operations of a utility's environmental surcharge. After hearing, the Commission may, by temporary adjustment of the surcharge, disallow any surcharge amounts that are not just and reasonable and reconcile past surcharge collections with actual costs recoverable pursuant to KRS 278.183(1).

The Commission issued a procedural schedule that provided for discovery, the filing of prepared testimony, an informal conference, and a public hearing. KU filed prepared direct testimony and responded to requests for information. On February 2, 2011, KU and Commission Staff ("Staff") participated in an informal conference to

¹ KU's environmental surcharge is billed on a two-month lag. Thus, surcharge billings for May 2010 through October 2010 are based on costs incurred from March 2010 through August 2010.

discuss the issues in the case. On February 22, 2011, KU requested that this case be submitted for a decision based on the existing record without a public hearing. Based on the absence of intervenors and finding good cause, the Commission will grant KU's request and decide this case based on the evidence of record without a hearing.

SURCHARGE ADJUSTMENT

The December 27, 2010 Order initiating this case indicated that, since over- or under-recoveries of allowable environmental compliance costs may have occurred during the period under review, the Commission would entertain proposals to adopt one adjustment factor to net all over- or under-recoveries. KU determined that it had a net over-recovery of environmental costs for the billing period ending October 31, 2010 of \$5,290,382.² It proposed that the net over-recovery be refunded to customers over six months, beginning in the second full billing month following the Commission's Order in this proceeding.³

The Commission has reviewed and finds reasonable KU's calculation of a net over-recovery of \$5,290,382 for the billing period covered in this proceeding. The Commission also finds reasonable KU's proposal to decrease the total jurisdictional environmental surcharge revenue requirement by \$881,730 for five months and \$881,732 for one month beginning in the second full billing month following the date of this Order. KU calculates that, for a residential customer using 1,000 kWh per month, the environmental surcharge billed will decrease by approximately \$0.69 per month to refund the net over-recovery over six months.

² Conroy Direct Testimony filed January 12, 2011 at 4.

³ Id. at 8.

RATE OF RETURN

KU provided the outstanding balances for its long-term debt, short-term debt, and common equity as of August 31, 2010, the last expense month of the review period. It also provided the blended interest rates for its long-term and short-term debt as of August 31, 2010.⁴ Using this information, along with the currently approved 10.63 percent return on equity,⁵ KU calculated an overall rate of return on capital, before income tax gross-up, of 7.84 percent.⁶ KU also provided the overall rate of return on capital reflecting the tax gross-up approach approved in Case No. 2004-00426.⁷

The Commission has reviewed KU's determination of the overall rate of return on capital and finds 7.84 percent to be reasonable. The Commission has also reviewed the determination of the tax gross-up factor and finds that it is consistent with the approach approved in Case No. 2004-00426. Therefore, the Commission finds that the weighted average cost of capital of 7.84 percent and the income tax gross-up factor of

⁴ Response to Commission Staff's Information Request dated January 12, 2011, Item 5b.

⁵ Case No. 2009-00548, Application of Kentucky Utilities Company for an Adjustment of Base Rates (Ky. PSC Jul. 30, 2010).

⁶ Response to Commission Staff's Information Request dated January 12, 2011, Item 5c, page 1 of 2.

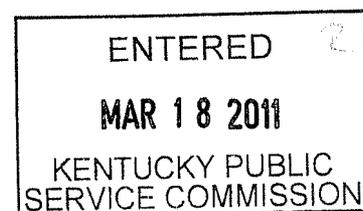
⁷ Case No. 2004-00426, The Application of Kentucky Utilities Company for a Certificate of Public Convenience and Necessity to Construct Flue Gas Desulfurization Systems and Approval of Its 2004 Compliance Plan and Recovery by Environmental Surcharge (Ky. PSC Jun. 20, 2005); and Response to the Commission Staff's Information Request in this proceeding dated January 12, 2011, Item 5c, page 1 of 2. In the response, KU determined that the income tax gross-up factor was 0.560, which would produce a tax grossed-up weighted average cost of capital of 11.04 percent.

0.560 should be used in all KU monthly environmental surcharge filings beginning in the second full month following the date of this Order.

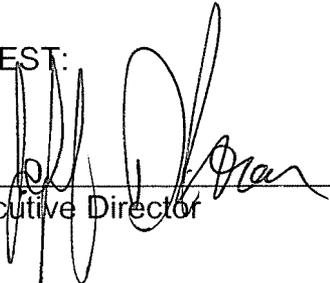
IT IS THEREFORE ORDERED that:

1. KU's request to submit this case for a decision on the existing evidence of record without a hearing is granted.
2. The amounts billed by KU through its environmental surcharge for the period from May 1, 2010 through October 31, 2010 are approved.
3. KU shall decrease by \$881,730 per month for the first five months and \$881,732 for the following one month its jurisdictional environmental revenue requirement determined in the month beginning in the second full month following the date of this Order, as discussed herein.
4. KU shall use an overall rate of return on capital of 7.84 percent and a tax gross-up factor of 0.560 in all monthly environmental surcharge filings beginning in the second full month following the date of this Order.

By the Commission



ATTEST:



Executive Director

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